

AIDE MEMOIRE

The Country Development Team-Timor-Leste (the CDT) hosted a Millennium Challenge Corporation (MCC) mission from May 6-May 17, 2019 to conduct due diligence on a potential project to improve commercial dispute resolution in Timor-Leste that is being considered for inclusion in an upcoming compact between the Government of Timor-Leste and MCC. The concept for improving commercial dispute resolution in Timor-Leste arose from the constraints analysis process and the root cause workshop conducted between the Government of Timor-Leste and MCC. To ensure that MCC and CDT build a compact that sustainably grows the economy, the CDT and MCC explored strategies for engaging the private sector during compact development.

Mission Overview

During the May 2019 mission, the CDT and MCC mission team met with over 100 relevant stakeholders to discuss challenges in commercial dispute resolution and importance of engaging private sector during compact development. Meetings included the President of the Court of Appeals, judges and staff of the Dili District Court and Court of Appeals, the Ministries of Justice, Commerce, and Legislative Reform & Parliamentary Affairs, an advisor to the National Parliament's legislative and judicial reform initiative, the Office of the Public Defender, the Legal Training Center and UNTL law school, lawyers, businesses, banks, associations and relevant NGOs and donor organizations.

Through these meetings, MCC and the CDT have been able to confirm that support for a compact project to improve commercial dispute resolution exists within the judiciary, key ministries, legal education providers, and the legal and business communities. In addition, a potential project appears to be well-aligned with new legislative and judicial reform initiatives within the Ministry of Legislative Reform & Parliamentary Affairs (MRLAP) and the National Parliament. MCC and the CDT also met with other donors to begin identifying complementary priorities that may enable greater project impact and sustainability. At this time, it appears that the timing of these other interventions would fit well with the project design timeline, and many stakeholders seem open to collaboration and discussion to ensure mutually supportive undertakings.

In addition, MCC's Finance Investment and Trade (FIT) representative worked with the CDT to familiarize them with the role of FIT and MCC's requirements related to engaging with the private sector throughout the compact development. As part of the process, the strategy of establishing a private sector advisory board was discussed with both CDT members and representatives from the business community identified as potential candidates, including at least one international firm.

Key Findings on Commercial Dispute Resolution

The meetings conducted during this mission confirmed and elaborated on previous findings in the constraints analysis and root cause workshop regarding the difficulty of enforcing contracts

through the judicial system and the limitations this constraint places on lending and investment. Building on prior findings, the team conducted focused discussions regarding specific obstacles to judicial resolution of commercial disputes and invited opinions from all stakeholders on potential solutions.

Throughout the meetings, stakeholders expressed broad consensus concerning the following points:

- 1) enforcing contracts in Timor-Leste is a painful and extremely slow process with a low chance of recovery;
- 2) some form of judicial specialization will be necessary to address delays in decision-making; and
- 3) legal education and qualification for judicial actors will need to be revised to improve the efficiency and quality of the judicial system, including in the area of commercial law.

An efficient, specialized forum for the resolution of commercial disputes was considered key to improving commercial dispute resolution. While there is broad consensus on the need for some form of judicial specialization to create such a forum, key stakeholders seem to have different concepts as to what specialization to undertake, how that specialization will be carried out, and which judicial actors should be trained and how. On this issue and any other area of potential project intervention, the views of all relevant stakeholders will need to be further consulted, elaborated, and reconciled as a potential project is developed.

A number of additional challenges were highlighted that will need to be considered in project design, including: slow service of process (notification); delays in scheduling hearings and frequent adjournments; limited functionality and training on the case management system; low Portuguese language literacy among judges, lawyers, and the parties and challenges in the use of Tetum in the judicial system; lack of formal alternative dispute resolution mechanisms; and lack of effective enforcement mechanisms due to the need for land and moveable asset registries. Although a subset of stakeholders identified important gaps in existing Timorese commercial law, these gaps were deemed either not critical to deciding the majority of commercial cases or slated to be included in the upcoming legislative effort in the National Parliament.

In addition, banks and businesses indicated a need for training in business and accounting skills for small and medium-sized enterprises and entrepreneurs in addition to improved commercial dispute resolution. They were indifferent as to whether formal arbitration processes would be preferable to an improved judicial system.

Potential Project Interventions

Following the mission, the CDT and MCC mission team agreed to continue exploring the development of a potential Commercial Dispute Resolution project (the CDR project). A comprehensive list of potential intervention areas, as discussed during the mission debrief, is included as Annex 1. The CDR project development process (as well as the project development process for the other projects) will also include further stakeholder consultations to obtain the input of those individuals or institutions whose participation is considered important for political

support, collaboration in project design, and coordination across government and in the donor community. This is particularly important for the CDR project, given the number of relevant stakeholders and the need for coordination across three branches of government.

Private Sector Engagement Strategy

There is a clear appetite and interest from the private sector to be involved and support the CDT during the development process. Building on this enthusiasm and MCC's requirement to engage with the private sector during compact development, this creates a strong foundation on which to build a private sector engagement strategy. As an example, one business leader cited a similar process with the Hotel Association and development of the USAID project as being quite effective and a possible model for the CDT. However, there are concerns from the CDT on composition, effectiveness of such an advisory board in current political climate and possibility that a board that includes civil society might be more effective in "nudging" the agenda and priorities.

Next Steps

MCC and the CDT agree to the following timeline for all project proposals, including CDR:

- Bullet Point Project Proposals in line with the MCC Template submitted by CDT to MCC by May 31, 2019;
- Full DRAFT Project Proposals in line with the MCC Template submitted by CDT to MCC by June 30, 2019;
- Final Project Proposals in line with the MCC Template submitted by CDT to MCC by July 31, 2019.

In addition, related to the strategy for engaging the private sector in the project definition and development phases, MCC and the CDT agree to the following:

- CDT will research further the Hotel Association and *Tourism for All* project development as a possible model;
- Private Sector Engagement Strategy to be submitted by June 2019, including detailed description of objectives, frequency of meetings, proposed candidates for advisory board and implementation timeline.

To further develop the CDR project, MCC will work through David Kassebaum as project lead and Amy Chambers as technical lead, while the CDT will nominate one or more individuals to work with David Kassebaum and Amy Chambers. Katherine Farley will support the CDT on issues related to private sector engagement during compact development and working toward a compact program that responds to private sector needs and feedback.

Acknowledged:

Ambassador Constancio Pinto
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ANNEX 1

Potential Project Interventions

In the debrief with the MCC and CDT teams on May 17, 2019, the following five possible areas of intervention were discussed for the potential Commercial Dispute Resolution (CDR) project. This list is neither exhaustive nor final but simply represents a summary of the initial discussions between MCC and the CDT after the mission. Based on the root cause analysis workshop and the recent consultations, it is clear that some form of specialized forum for the resolution of commercial disputes - the primary intervention area - is fundamental to achieving the theory of change envisioned for this project. One or more of the options described (or a similar option that achieves the same goal) under the primary intervention area should be included in the project proposal for a compact project to have the envisioned impact on the growth of the economy. The CDT will continue to refine both the potential intervention areas and the activities associated with each in collaboration with MCC and work with key stakeholders to determine whether the decisions necessary to develop an impactful project can be achieved on a compact timeline. As part of the project development process, the CDT aims to submit the first draft of a refined version of the project proposal to MCC by May 31, 2019.

List of Potential Intervention Areas

- Primary Intervention: Support establishment of an efficient, specialized forum for the resolution of commercial disputes
- Secondary Intervention Areas:
 - Support reforms to legal education and certification to expand and strengthen the legal profession (judges, prosecutors, public defenders, and private lawyers)
 - Support development of secure forms of collateral to facilitate lending
 - Support efforts to develop and implement the commercial legal framework
 - Build capacity in business and accounting skills for SMEs

Primary Intervention: Support establishment of an efficient, specialized forum for the resolution of commercial disputes.

Description: This intervention could include support for one or more of the following: (1) a specialized court of division within the judicial system, (2) establishment of domestic arbitration, and (3) creation of a fast-track judicial or arbitration-based forum for ruling on simple commercial disputes, particularly geared towards small and medium-sized businesses. The objective is to establish a forum for obtaining fair decisions on the basis of commercial law within a reasonable timeframe that is accessible to SMEs and has the confidence of foreign investors.

The scope and viability of the intervention is dependent the decision of the Government of Timor-Leste to establish a specialized forum for commercial disputes. Based on conversations with relevant stakeholders, it is believed that this issue may be addressed in anticipated legislation on the organization of the judiciary and alternative dispute resolution. However,

specific activities cannot be determined without further information from the Government of Timor-Leste regarding the timing and content of this legislation. Depending on these decisions by the Government of Timor-Leste, this intervention could include one or more of the following options:

Option 1: Parliament passes the Law on the Organization of the Judiciary, which establishes the High Administrative, Tax, and Audit Court, and the Superior Council of the Judiciary gives the High Court jurisdiction over commercial disputes.

Potential Activities:

- Advising on the establishment of rules of procedure for the High Court that ensure efficient case management
- Training judges selected to sit on the High Court in commercial law and case management
- Supporting a program of advisory services for these judges within the High Court
- Development and training on ICT case management system for judges and court staff
- Working with court staff and relevant government authorities to improve the efficiency of service of process (notification)
- Socialization of the new forum within the business community

Option 2: The Superior Council of the Judiciary establishes separate divisions within the courts (or at least within Dili District Court) for criminal and civil matters and designates specific judges to serve in these divisions.

Potential Activities:

- Advising on the revision of rules of procedure to improve the efficiency of case management
- Training the selected judges in commercial law and case management
- Supporting a program of advisory services for these judges within the court
- Development and training on ICT case management system for judges and court staff
- Working with court staff and relevant government authorities to improve the efficiency of service of process (notification)
- Socialization of the new forum within the business community

Key Considerations:

- Collaboration with other donors: Both Portugal and Brazil are currently supporting advisory services within the district courts and Court of Appeals. Potential project activities should complement and coordinate with these organizations.

Option 3: Parliament passes a new law on Alternative Dispute Resolution (ADR) aligned with the UNCITRAL Model Law that provides for the establishment of arbitration for commercial disputes with limited, non-substantive grounds for appeal of arbitration decisions in court.

Potential Activities:

- Advising on the establishment of qualifications, certification, and a code of ethics for arbitrators
- Advising on the establishment of rules of procedure for arbitration cases to ensure objectivity, transparency, and efficient case management
- Training arbitrators in commercial law and arbitration procedures
- Training judges on the grounds for appeal of arbitration decisions
- Working with court staff and relevant government authorities to improve the efficiency of service of process (notification)
- Socialization of the new forum within the business community
- Advising on the adoption of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards
- If the ADR law includes mediation, support establishment of a formal mediation center for commercial disputes, court-based or within a private institution such as CCI-TL, to reduce the caseload of the courts or arbitration

Option 4: The legislative and judicial reforms described in Options 1 and 3 also allow for the establishment of a fast-track procedure for simple commercial disputes, such as through a court of first instance with appeal to the High Court or a simplified arbitration procedure.

Potential Activities:

- Advising on the establishment fast-track, simplified rules of procedure to ensure efficient case management in these cases
- Training the judges or arbitrators selected to hear these cases on commercial law and case management
- Supporting a program of advisory services for these judges or arbitrators
- Development and training on ICT case management system for judges and court staff (if applicable)
- Working with court staff and relevant government authorities to improve the efficiency of service of process (notification)
- Socialization of the new forum within the business community

Secondary Intervention Area 1: Support reforms to legal education and certification to expand and strengthen the legal profession (judges, prosecutors, public defenders, and private lawyers).

Description: This intervention would support improvements in legal education to ensure all legal practitioners have a standard base of knowledge and understanding of the law, including commercial law. It would likely entail changes to the curriculum of the Legal Training Center (LTC) and could extend to law schools. It could include the establishment of professional certification for all legal practitioners, such as through a standard bar exam and establishment of a bar association. It could also support changes to how and when legal practitioners receive

practical training in a specific profession to facilitate new pathways to filling vacancies in the judiciary, prosecutor's office, and public defender's office.

Potential Activities:

- Support in revising the educational requirements for legal practitioners in Timor-Leste, such as amendments to the mandate of the LTC to make it mandatory for all legal practitioners (judges, prosecutors, public defenders, and private lawyers)
- Support for establishment of new pathways and criteria for entering different legal professions to increase the pipeline of new judges, prosecutors, and public defenders while ensuring all new hires are qualified for these positions
- Establishing a Timor-Leste bar association and development and implementation of a standard bar exam for all legal practitioners
- Working with the LTC (and possibly UNTL and other law schools) to revise its curriculum to include a greater focus on commercial law
- Developing training materials on commercial law in Portuguese and Tetum
- Support for MoJ initiative to develop legal Tetum and the translation of laws, textbooks, and legal information for the business community into Tetum

Key Considerations:

- Anticipated legislative reforms: The mandate of the LTC is governed by its statute, which is currently under revision by the MoJ. The scope of this intervention will depend on the content of that law and when it is enacted.
- Collaboration with other donors: While various donors have provided occasional trainings in substantive areas of the law, no other organizations are known to be working on this issue. The LTC expressed interest in entering into some form of partnership with universities or other organizations with training capacity.

Secondary Intervention Area 2: Support development of secure forms of collateral to facilitate lending.

Description: Discussions with banks in Timor-Leste revealed that one of the key impediments to lending is the lack of legislation and institutions for establishing secure forms of collateral for a loan. This intervention would support the implementation of land and moveable property registries to enable lending against these assets.

This intervention is dependent on passage of the decree-law on the land registry and enactment of a secured transactions law covering moveable property. A draft decree-law on the land registry is believed to be in the process of finalization in the MoJ. A draft secured transactions law was previously prepared by MECAE, but its status is unknown. The scope and viability of this intervention cannot be determined until the timing of these anticipated reforms is known.

Potential Activities:

- Work with the Banco Central to establish a moveable property registry and procedures for securing a lien against a moveable asset
- Training for judges and court staff in enforcement actions, including procedures for the identification, seizure, valuation, and sale of assets
- Socialization of new land and moveable property registry laws and procedures for all judicial actors, banks, and the business community

Secondary Intervention Area 3: Support efforts to develop and implement the commercial legal framework.

Description: The Parliament has adopted a legislative agenda that includes further development of the commercial legal framework. These reforms are expected to take place in the next 2-3 years (and beyond) with the support of the UNDP and other donors. This intervention would focus on supporting the effective implementation of new commercial laws by educating legal practitioners and the business community on new developments, but the project could also provide support as needed during the drafting phase.

Potential Activities:

- Advising relevant ministries and Parliament on draft legislation (if needed)
- Convening stakeholders for consultation on draft laws (if needed)
- Adapting training materials and curriculum at the LTC and law schools to include newly enacted commercial laws
- Training judges and lawyers on new developments in commercial law
- Socialization of new commercial laws within the business community

Key Considerations:

- Collaboration with other donors: Many donors have previously advised on the drafting of commercial laws, and these organizations will likely continue this support in the future. Project activities should be designed to complement these efforts.

Secondary Intervention Area 4: Build capacity in business and accounting skills for SMEs.

Description: Banks in Timor-Leste expressed concern that they do not receive loan proposals with sufficient sophistication to meet their internal standards for loan evaluation, particularly in the area of accounting, and that businesses use a wide range of accounting standards. This intervention would support improved business and accounting skills for SMEs with the specific objective of improving access to finance.

Potential Activities:

- Establish or expand existing services to train SMEs in business and accounting skills
- Work with the GOTL to establish uniform basic accounting standards for Timor-Leste

Key Considerations:

- Collaboration with other donors: During the debrief, no less than eight organizations were identified that already provide this type of support to businesses. More information is needed to understand the content of these services and why they are insufficient to enable businesses to develop good loan proposals.
- Any such intervention should be aligned with the potential skills project that has also been proposed for this compact.